



# Mittelstand Insights Review

The Importance of Addressing Succession Challenges

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## Executive Summary —

Every year Ballast conducts research on how the private sector can improve its engagement with policymakers. This year, our research centers on what policymakers want to see from companies on Environment, Social and Governance (ESG), and how perceptions of ESG differ internationally. In our conversations with German policymakers, one issue that surfaced, and is key to understanding ESG in the German context—is the economic and social-cultural importance of the German Mittelstand. In this first piece on ESG, we examine the importance of the Mittelstand and the need to address succession challenges.

# What Is Mittelstand?

Mittelstand is the “hidden champion” of the German economy. They encompass the small-to-medium sized enterprises (SMEs) in the DACH region (Germany, Austria, and Switzerland). These are often family-owned (Familienunternehmen), spanning multiple generations with specialized manufacturing productions that form the backbone of the German economy.

The organizational characteristics of these companies are very well-studied, with research specifically emphasizing their incorporation of set family values when enacting an “enlightened” capitalism governance model.<sup>1</sup> These companies generate one-third of the total turnover of German companies and account for 34.4% of all employees subject to social security contribution,<sup>2</sup> solidifying their place as a major pillar of Germany’s robust business society.<sup>3</sup> Moreover, these companies hold a reputation for their crisis resistance abilities,<sup>4</sup> especially through managerial and technological innovations,<sup>5</sup> such as during the economic crash of 2008, the COVID-19 crisis in 2020, and the Ukrainian invasion earlier this year.

## A Succession Challenge

In our research this year, policymakers in the DACH region express concerns about the forthcoming succession crisis these companies will face. According to research by KfW,<sup>6</sup> 1.5 million business owners are aged 55 years or older, meaning that in the coming years, upwards of 76,000 Mittelstand companies will require suitable successors. Nearly half of these businesses are expecting a transition in the next two years.<sup>7</sup> Fifty-six percent of these companies plan to keep it in family,<sup>8</sup> while 13% are considering a sale rather than passing their companies down the generational line.

While COVID-19 has reshifted priorities, the issue of succession remains unchanged. Mittelstand owners are increasingly looking for outside resources and expertise, and policymakers believe that incoming leaders should continue to place a focus on ESG as management transitions.

*“The most worrying issue in any business leadership is the succession in the years to come. We have a lot of ownership changes that still don’t have successors. The equity market is taking over but ESG is a big guiding principle for these companies, especially the S, so this is a time to refocus our ESG goals and figure out what our common objective is.”*

Elected Business Representative for a German Association

Part of the reason for the succession crisis is due to the aging population in Germany and a refocus of priorities by the new generation.

*“The new generation have never shown any interest or the person in charge has never shown them the ropes or the process of what goes into the business.”*

German Human Resource Specialist



## ESG Exemplars

Mittelstand has traditionally shown to be “crisis resistant” and part of its resistance is attributed to their ability to act unified<sup>9</sup> and treat their workers well even during a crisis.

DACH policymakers point to the Mittelstand as examples of what “good” social engagement looks like.

*“In general, they take care of their workers, they go out of their way to make sure everyone stays on during crises. The executives will often take a pay cut so that everyone gets paid.”*

Former Senior German Federal Advisor

*“They treat their employees so well; addressing an oft missed S & G in ESG. You sustain your business for so much longer this way.”*

Senior Diplomat to Germany

## Long-Term Relationships Are Key

Leaders want to see long-term partners who understand and are attuned to the local culture, and who they believe they can trust.

*“I don’t consider my children because I don’t want them to run it to the ground... but I also won’t invite anyone to be a partner. I want partners who understand my work.”*

CEO, German Familienunternehmen

*“You cannot come in and expect the world, there are a lot of misunderstandings about German culture. It is going to take a lot longer than you think to build the relationships that you want to build.”*

Trade Representative to Germany

*“No Mittelstand owner is going to invite you in as a partner if you are just coming in for five, seven years and sell it. They have to really really trust you. They want a longer term relationship.”*

Senior Diplomat to Germany



## Conclusion ---

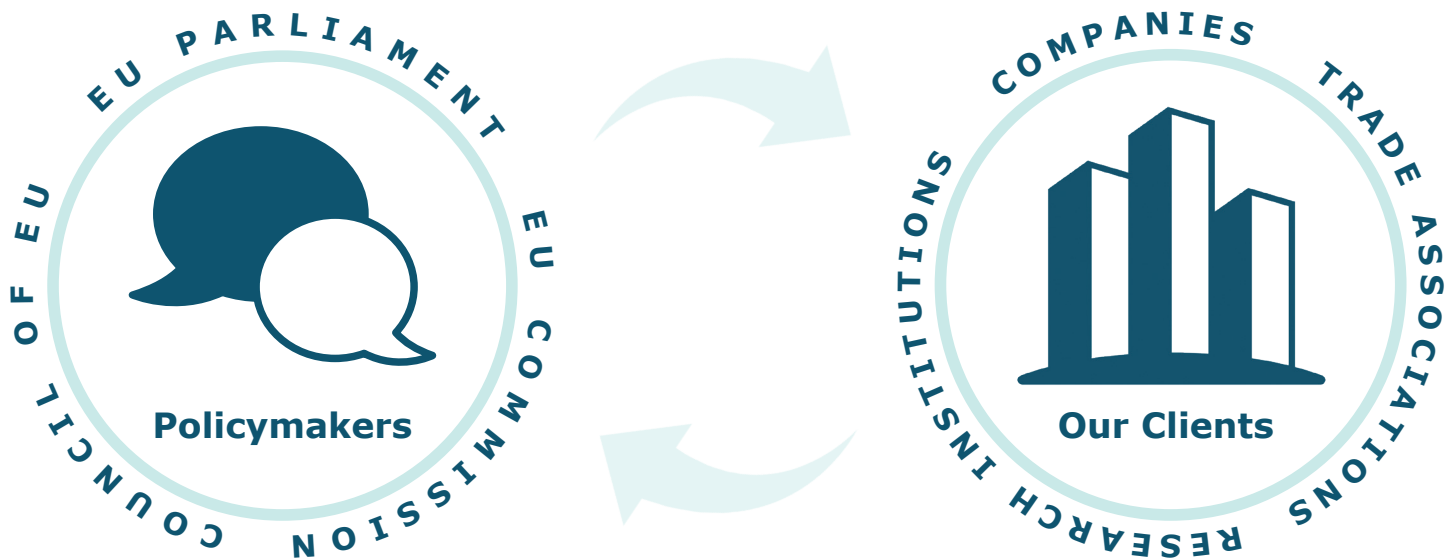
Policymakers believe that the changing demographic of Germany's business community presents a growing opportunity for leaders to continue to infuse ESG principles into their organizations. With succession such an important social issue for the German Mittelstand, the necessity of forward-thinking leadership that is both aware of the cultural significance of these unique dynamics and able to keep up with a shifting global dynamic is increasingly clear. The structure of these Familienunternehmen has provided a rare perspective when it comes to retaining talent and remaining resilient in times of crisis. Policymakers want to ensure that is preserved, specifically noting the importance of treating employees well and maintaining long-term relationships during times of change.



# About Ballast Research

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Ballast Research gathers direct feedback from policymakers, investors, and other key stakeholders to help inform, direct, and correct the engagement they receive from companies.



## Our Promise

**Confidentiality:** All participation in our research is confidential and not for attribution.

*“ This deep-dive, customized research is invaluable for understanding what policymakers think of us and need from us. The insights are another important tool we use to inform our thinking on how to engage, and the data illuminates where we can do better.*

Head of US Communications, Fortune 10 Company *”*

# Credits

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